
12th March 2010

A Better Deal for Consumers: Consultation on proposal to ban the use of bills of sale for consumer lending

Community Development Finance Association response

The Community Development Finance Association (**cdfa**) is pleased to respond to BIS's consultation to propose to ban the use of bills of sale in consumer lending.

The **cdfa** is responding on behalf of its 68 members comprised of Community Development Finance Institutions (CDFIs). Please see Annex for a full list of members. CDFIs are non-commercial social enterprises which deliver an appropriate financial services to those in greatest need. CDFIs serve three markets: third sector/social enterprise; micro, small and medium businesses in disadvantaged communities and financially excluded individuals, providing credit where access to finance has been denied by mainstream financial institutions.

Our response has been instructed via direct consultation with the membership.

The majority of our membership do not use bills of sale as a form of security, and few, if any, use bills of sale for personal lending. However, there is some prudent use of the practice amongst a small number of members who provide credit to microenterprises who are either unincorporated or operating as sole traders.

Defining 'Consumer Lending'

As a preamble to our response, we feel it necessary to identify the need to clarify what is meant by the term 'consumer lending', which is not fully and clearly defined in the consultation document.

Advice from BIS indicates that the focus of the consultation is on banning the use of bills of sale for consumer lending with no intention to ban Bills of Sale for business lending, including for commercial loans to sole traders. However, BIS also recognises a grey area in distinguishing between commercial and consumer lending when it comes to sole traders and informal businesses.

The Office of Fair Trading's (OFT) consumer credit regulations apply to agreements where the borrower is an individual, a sole trader, and a partnership with three or fewer partners or an unincorporated association.

Therefore, it is advisable to clearly distinguish between consumer lending for personal use versus consumer lending for entrepreneurial purposes.

BIS must take care to ensure that the use of bills of sale for lending to sole traders and unincorporated businesses is not insinuated into the definition of exploitative 'consumer lending' that this consultation seeks to redress.

Further distinctions in lending to sole traders and unincorporated entities must be appreciated to ensure that this activity is not inadvertently relegated to the 'consumer lending' category, even in cases where personal assets are secured using bills of sale for business purposes.

It is also important to distinguish between for-profit lenders – especially potentially exploitative ones, such as log book lenders – and not-for-profit lenders such as CDFIs who are acting in a socially responsible manner.

To bypass the 'grey area' that exists between personal consumption and personal for business loans an exclusion from the ban to not-for-profit social lenders, namely CDFIs should be introduced.

Responses to consultation questions

What is the problem?

Q1. The Government would welcome further evidence about the current nature of the bills of sale consumer lending market [...]

Few CDFIs routinely use bills of sale for their 'consumer lending' activities. Whilst it appears that no CDFIs use bills of sale for strictly personal/consumer lending, a few CDFIs occasionally rely on bills of sale in order to enable them to make loans to high risk informal businesses/sole traders, which may, as stated above in the 'Defining Consumer Lending' section, are captured by some definitions of 'consumer lending.'

For a sole trader or individual looking to set up a business, their own personal assets may be the only security available. The use of a bill of sale allows the CDFI to advance a loan and offer support to a business that otherwise would be unable to access finance. Examples of this type of security include taking ownership of plant machinery or vehicles as collateral for advancing funds. Restricting or banning the use of bills of sale for this type of lending would thereby impact the very people CDFIs were set up to help and in the process driving them elsewhere, stifling innovative business creation at the poorest end of the market.

As this consultation identifies, it is high cost exploitative consumer activity, in particular by log book lenders, requiring correction, whether through reform, greater regulation or an outright ban.

Proposals

Option 1: Do nothing beyond current legislation and regulatory activity

Q2. We would welcome evidence on the extent of consumers' understanding of the terms of bills of sale, and their options in the event of default should they wish to prevent the seizure of the secured asset.

No comment

Q3. Is it fair and reasonable to have fewer protections for consumers borrowing money under a bill of sale than under other forms of consumer credit agreement including hire purchase agreements?

No. All forms of security and potential ownership of a customer's property should have significant consumer protection processes in place. All of these should be protected via the Consumer Credit Act

Q4. Will the implementation of the Consumer Credit Directive, combined with OFT guidance, provide sufficient additional consumer protection in this area? If not, what other measures (not covered in this consultation) would you suggest to improve consumer protection?

This may work, provided that the Consumer Credit Directive rules are stringent enough and enforceable. If there is any danger of a loophole being exploited by the log book lenders whereby less protection is given to customers in relation to taking other forms of security then this 'light touch regulation' would not help to address the problems described in this consultation.

Option 2: Introduce a voluntary code of practice or other non statutory requirements

Q5. Would a voluntary code of practice, if adopted by bill of sale lenders, coupled with ongoing enforcement action, provide sufficient additional protections for consumers?

The **cdfa** would support the introduction of a code of practice, but believe a voluntary code would not have the teeth to adequately protect consumers. A compulsory code of practice may be more effective as long as meaningful penalties are in place for malpractice.

Q6 Would a code of practice requirement to register a bill of sale loan agreement with online electronic asset finance registers provide sufficient protection for third party consumers?

No comment.

Option 3: Reform bills of sale legislation to make it more appropriate for consumer lending

Q7 *To what extent would reform of the legislation rectify the problems identified in relation to bills of sale?*

Proposed reforms, if provided as suggested in the consultation, would certainly go some way towards addressing the main issues associated with bills of sale, and would provide the appropriate level of regulation and support for customers.

In regards to section 82 specifying possible reform practices, all the suggested changes seem warranted and acceptable. Prior care, however, must be taken to ensure that those CDFIs complying with other regulations are not overly burdened. Regulation should be in place for log book lenders and providers of credit for consumables. CDFIs should not be bundled into those for whom the spirit of these proposed changes are meant, that is, the responsible use of bills of sale for business lending by CDFIs.

Q8 *If you consider that a bills of sale type instrument for consumer lending should be preserved, what would make a credible package of reform measures to ensure sufficient consumer protection?*

A bills of sale type instrument for should be preserved only for certain types of consumer lending by certain lenders. To ensure sufficient consumer protection, only not-for-profit lenders providing affordable credit to vulnerable consumers should be permitted to use such an instrument.

Q9 *What might be the unintended consequences of this option, including the implications for access to affordable credit for vulnerable consumers?*

There maybe unintended consequences of burdensome regulation for those CDFIs that use bills of sale. CDFIs are often the only option available to vulnerable consumers in accessing fair and affordable credit. Restrictions on not-for-profit, affordable credit providers could hamper the ability of some CDFIs to adequately serve financially excluded markets.

A possible consequence of this could be some retraction of credit provided to high risk micro-enterprises and sole traders, resulting in borrowers using high cost or illegal lenders or making a decision to abandon enterprise plans completely.

Q10 *What might be the costs to lenders of this reform and adopting a new secured lending instrument?*

CDFIs willingly comply with Consumer Credit Act and would welcome new secured lending instruments under this rubric.

Option 4: Ban the use of bills of sale for the purpose of consumer lending

Q11 *Should bills of sale for consumer lending be banned?*

The government must be extremely careful in introducing a total ban of bills of sale. Whilst it maybe appropriate to ban them for irresponsible log book lenders insurances need to be made that this method will not be banned for CDFIs lending to sole traders and unincorporated entities, unless some suitable replacement is devised. (See section above, Defining 'Consumer Lending')

Q12 *If bills of sale for consumer lending were banned, are there real alternative forms of borrowing available to consumers?*

Yes. CDFIs exist to deliver affordable finance to individuals and businesses unable to access credit from mainstream sources.

Expansion of the CDFI sector is essential to help fill the gaps left behind by the log book lenders. Government should support CDFIs to ensure that this alternative becomes entrenched and widely available as the only alternative between mainstream finance and high cost or illegal lenders.

Q13 *What would be the benefits and risks of a ban on the use of bills of sale to consumers?*

There is a real risk of vulnerable borrowers recognising no alternative other than high cost or illegal lenders.

An outright ban on bills of sale would increase the number of consumers seeking finance. Unless the scale and reach of CDFIs are extended, these consumers will be forced to access another form of exploitative high-cost or illegal lenders.

Q14 *What might be the costs to lenders of using alternative methods of lending?*

For CDFIs that use bills of sale as a type of security which enables them to lend to consumers for business purposes, there is likelihood that such credit would simply be curtailed. Therefore, the real costs to the CDFI are relatively small.

However, the loss to the individual unable to access affordable credit would be particularly high. The greater costs in this sense are to society as a whole, and not the private costs of CDFIs.

Q15 *What might be the unintended impacts on consumers and lenders of a ban on the use of bills of sale?*

Curtailling prudent use of bills of sale in CDFIs to sole traders and informal businesses who are unable to access affordable finance from other sources will impact on businesses creation and entrepreneurship in the UK's most deprived wards.

In a broader sense when moderating/changing the law surrounding bills of sale the government must be aware of driving vulnerable borrowers into the hands of illegal lenders or extortionate doorstep providers of credit. Borrowers using log book lenders are often vulnerable people with nowhere else to turn. If no viable alternative is sought by the government, such as capitalising the CDFI sector, previous log book users may be driven underground finding themselves in a situation with no protection in an unregulated market. Greater investment needs to be channelled towards the CDFI sector as a viable alternative bringing affordable credit to vulnerable consumers.

Q16 *Of the 4 options proposed, which do you prefer?*

A solution is needed which prevents the log book lenders exploiting vulnerable consumers whilst also allowing ethical, socially minded lenders to use this type of security in cases where responsible lending requires some form of security. The **cdfa** is certainly against log book lenders who charge a high level of interest to vulnerable consumers and agree with the need to overhaul this outdated legislation. Log book lending against individuals' cars needs to be controlled and legislation put in place to protect consumers.

It is important that with any legislation that is considered CDFIs are not grouped together with traditional log book lenders. CDFIs demonstrate that there are ethical lenders operating in the consumer/informal business markets who do use bills of sale as a legitimate form of security. Banning

bills across the board will lead to these consumers who are already disadvantaged unable to access the affordable credit that CDFIs provide.

Conclusion

It would be a great mistake to do nothing beyond the current legislation. Within the purely personal lending spheres bill of sale use is exploitive and damaging to already vulnerable borrowers. We would support either an outright ban of bill of sale use for personal borrowing purposes only, a restructuring of the law bringing it up to date and subordinate to the Consumer Credit Act or the introduction of a compulsory code of practice for log book lenders only.

- Allow CDFIs to continue to use bills of sale to fund unincorporated businesses or sole traders.
- Overhaul and update the bills of sale regulation allowing the Consumer Credit Act to supersede any Bill of Sale agreement, bringing legislation up to date and protecting consumers. A compulsory code of practice outlining ethical practices in the use of bills of sale may also be introduced with clear ramifications outlined in the case of a breach.
- Greater investment needs to be put into viable social alternatives such as CDFIs, to help build a landscape where vulnerable consumers can access affordable credit, moving them away from log book lenders, doorstep lenders and loan sharks.

March 2010

Annex: List of **cdfa** members

ABI Associates - Faith in Business	Impetus
Acorn Fund - Hull Business Development Fund	Innovative Finance - Hastings Trust
Aspire Microfinance	Isle of Wight Lottery - Opportunity Society
Aston Reinvestment Trust (ART)	Key Fund Yorkshire
Bees Knees	Lancashire Community Finance
BIGInvest	Leicestershire Moneyline
Black Country Reinvestment Society (BCRS)	London Rebuilding Society
Bridges Community Ventures	MCF Loans
Bristol Enterprise Development Fund	Merseyside Special Investment Fund
Business Enterprise Fund	Moneyline Greater Manchester
Business Finance North West (BFNW)	Moneyline Yorkshire
Business Finance Solutions	Norfolk & Waveney Enterprise Services (NWES)
Capitalise Business Support	North London Enterprise Credit Union
Charity Bank	North Staffordshire Risk Capital Fund
Co-operative and Community Finance	Plymouth Small Business Fund
Coventry & Warwickshire Reinvestment Trust	PRIME
Croydon Enterprise Fund	Prince's Trust
Cumbria Community Asset & Reinvestment Trust	Project North East (PNE)
Donbac	Robert Owen Community Banking Fund
DSL (Development Strathclyde Ltd)	Rootstock
East Lancashire Moneyline (ELM)	Scotcash
East London Small Business Centre (ELSBC)	Shoreline Housing Partnership
Enterprise Loans East Midlands	Sirius
FACT 2006	Social Investment Scotland (SIS)
Finance South Yorkshire	South Coast Moneyline
Five Lamps Organisation	South West Investment Group (SWIG)
Foundation East	Spirit of Enterprise Loan Fund
Fredericks Foundation	Street UK
Fredericks Gloucestershire	StreetNE
Fredericks Wessex	The Social Enterprise Loan Fund (TSELF)
Futurebuilders England	Triodos Bank
GLE oneLondon	Ulster Community Investment Trust (UCIT)
Goole Development Trust	WEETU - Full Circle Fund
HBV Enterprise	West Yorkshire Enterprise Agency